



San Diego City Attorney **MICHAEL J. AGUIRRE**

NEWS RELEASE

FOR IMMEDIATE RELEASE: *August 25, 2006

Contact: Maria Velasquez, Communications Director (619) 235-5725 (direct line) mvelasquez@saniego.gov

AGUIRRE CALLS FOR FURTHER EVALUATION AND MORE PUBLIC INPUT ON PORTIONS OF KROLL RECOMMENDATIONS

San Diego, CA: City Attorney Michael Aguirre called for intense public engagement on certain recommendations contained in the \$20.3 million Kroll Report and embraced by Mayor Sanders at a press conference yesterday.

Aguirre said that he agreed with many of the remediation measures recommended in the Kroll Report/Mayor's Reform Plan, but there are some that require significant changes to the San Diego City Charter and therefore require broader public input.

"Some of Kroll's proposed changes amount to substantial changes in the City government, and many move power away from elected officials and out of the hands of the electorate," Aguirre said. "These are issues that need to be properly reviewed by the public. It is not appropriate to unilaterally implement such significant changes without the proper public discourse at a series of community meetings."

Council President Scott Peters set a September 6, 2006 meeting of the San Diego City Council to decide whether to support the proposed recommendations. In the Kroll Report, Peters and other members of the City Council were found to have acted negligently in approving false and misleading information on the City's financial statements.

The following are the specific areas that the City Attorney believes need further review before adoption of the recommendations contained in the Kroll Report/Mayor's Reform Plan. They are numbered as they appear in Appendix M of the Kroll Report:

1. REORGANIZATION OF FINANCIAL REPORTING

The City Attorney believes that the reorganization of the financial reporting structure is, in fact, ineffective because it continues the very practices that allowed the City to decline into its current financial condition. Placing key positions in the City's financial reporting structure – including the Comptroller, Director of Financial Reporting, and the Director of Planning, Budget and Financial Analysis – under the
(MORE)

Chief Financial Officer removes the independence required to ensure the accuracy of the financial reporting. This is an issue that will require input from the public, research of best practices throughout the United States, and a debate within the City.

7. ENSURING COMPLETENESS OF DISCLOSURES: DISCLOSURE PRACTICES WORKING GROUP (DPWG)

The City Attorney does not support the recommendation regarding the composition of the Disclosure Practices Working Group (DPWG). The DPWG was created by ordinance on the recommendation of Vinson & Elkins and has functioned since late 2004. Under the ordinance, the DPWG is chaired by the City Attorney and the other members include the City Manager, Auditor and Comptroller, and City Treasurer. Kroll's principal recommendation is that the CFO be added to the DPWG as an "official" member and serve as chair. Currently, the CFO is already an "official" member of the DPWG because, under the strong mayor form of government, the City Manager slot was assumed by the Mayor.

As to the recommendation that the CFO chair the DPWG, the City Attorney believes this is contrary to the very purpose of the group. The DPWG's primary function is insure compliance with the federal securities laws and to serve as a check on the representations being made to the investing public by City officials. As Kroll correctly notes, the CFO has the responsibility of ensuring the accuracy of the City's financial disclosures. What Kroll fails to appreciate is that the DPWG was created precisely to evaluate those disclosures, essentially checking to make sure that the CFO has adequately discharged his responsibilities. To have the CFO checking his own work creates the potential for the DPWG to become a rubberstamp on the City's disclosures.

The primary purpose of the DPWG is legal compliance. Kroll tacitly acknowledges this by suggesting that the City's outside disclosure counsel be made an "ex-officio" member of the group. It is common sense to have the City Attorney, as the legal head of the City government, chair a body that serves an inherently legal function.

8. INDEPENDENT AUDITOR GENERAL

The City Attorney's Office is not opposed to the concept of a truly *independent* auditor general. However, the office as outlined by Kroll and adopted by the Mayor raises serious concerns. The Auditor General, as proposed by Kroll, will be nominated by the Mayor and confirmed by the Council. Therefore, the Mayor's office which has control and oversight of the City's budget and therefore, is acutely aware of the City's budgetary constraints, will oversee the person responsible for disclosing a true and accurate account of the City's financial health. This is the exact structure that was in place when the previous disclosure failures occurred. In order to be truly independent the Auditor General should be an elected position which will insure that the Auditor General is answerable to the public. Further, as proposed, the Auditor General may be removed by a three-quarters vote of the City Council. This raises serious concerns because the same elected officials that have been found to have acted negligently in our securities disclosure practices will oversee the person responsible for meeting the City's disclosure obligations.

(MORE)

9. AUDIT COMMITTEE

The City Attorney is opposed to the recommendation to establish a three-member Audit Committee. The creation of such an appointed body empowered with the legislative authority to, in effect, control the financial condition of the City is improper. It is no secret that the City of San Diego has recently experienced a disastrous situation with the implementation and operation of the Kroll Audit Committee.

The fact that the City Council is slated to confirm Mayoral nominations calls into question the independence of the Audit Committee members.

The second problem with this recommendation: the Kroll report found that five current City Council members acted with negligence in approving financial statements that included false and misleading information to public markets. The City Attorney believes that four sitting City Council members – specifically Council President Scott, Council members Brian Maienschein, Jim Madaffer and Toni Atkins – should play no role in choosing and exerting employment control over the members of such an Audit Committee.

Perhaps the most significant problem with such an Audit Committee is that a significant amount of power would be removed from the hands of elected officials and put into the hands of political appointees. In short, this creates an unelected and undemocratic branch of government.

The need for an Audit Committee can be easily resolved if the City Council performs the duties assigned to it. Specifically, the City Council offices receive briefs on the City's financial information by numerous layers of City staff. If the City Council members and City Council staff performed the due diligence expected of them by the San Diego City Charter and the San Diego Municipal Code, all concerns will be accurately identified and addressed.

The City Attorney believes that the Office of the Independent Budget Analyst can also handle the functions recommended for the Audit Committee.

10. SELECTION AND RETENTION OF AUDITORS

The City Attorney's office does not support Kroll's recommendation for selection and retention of auditors for the same reasons the City Attorney does not support an Audit Committee. In order to be a truly *independent* auditor, this position should be an elected position, not an appointed position. An independent auditor should report and answer to the people of the City of San Diego, not to the Office of the Mayor.

Further, the recommendation to commit to a five-year contract for the independent auditor unnecessarily commits the City of San Diego to possibly millions of dollars. The City of San Diego has already spent in excess of \$20 million dollars for the Kroll audit report.

(MORE)

18. SDCERS LEGAL COUNSEL

In recommending that SDCERS continue to retain its own “independent” legal counsel, Kroll makes reference to the intentional underfunding of the employee pension system under which that system’s interests were subordinated to the City’s interests as the reason to provide SDCERS with “independent” legal counsel. In so doing, Kroll misapplies the concept of independence. In order to be free of undo influence, a public lawyer should be independent from the appointing authority. In other words, a public lawyer cannot be truly independent if the same people he or she is advising have the power to modify and/or terminate that lawyer’s employment. The framers of the San Diego City Charter recognized this truism in deciding to have an independently *elected* City Attorney. These same framers mandated that the elected City Attorney serve as the chief legal adviser the all City departments, including the Retirement System. Since the adoption of the San Diego City Charter until 1997 the elected San Diego City Attorney served as the chief legal adviser to SDCERS. It was when the attorney advising SDCERS lost her independence and aligned herself with the Board that the “subordination of the system’s long term financial interests” occurred. Only by re-installing the truly independent, elected City Attorney as chief legal counsel for SDCERS, can the citizens of San Diego be assured that their interests will be protected.

17. RETENTION OF SDCERS AND CITY ACTUARY

The Recommendation set forth by Kroll states that the City should retain an auditor to review the SDCERS financial information every three years. The City Attorney believes that the City should retain an auditor to review the SDCERS financial statements on an annual basis.

24. OVERSIGHT BY MONITOR

The City Attorney’s office does not support the recommendation to hire a monitor to oversee the remediation process. The Mayor’s remediation plan says it will cost \$3 million to \$4 million over the next three years to monitor the remediation plan. It should be noted that Kroll currently serves as the Independent Monitor of the Los Angeles Police Department and has performed this role since 2003. Kroll has billed the City of Los Angeles over \$11 million to perform this function.

The monitoring function can be effectively performed by the City Council, the Mayor and the City Attorney’s office. The role of the City Council is to ask the right questions, to ensure that the remediation process is being implemented. The City of San Diego does not need to expend an exorbitant amount of money to monitor the process for which its current administration can perform.

###